



September 29, 2017

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RE: Proposed Statement on Auditing Standards, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA*

Ms. Hazel:

Eide Bailly LLP appreciates the opportunity to comment on the Proposed Statement on Auditing Standards, *Forming an Opinion and Reporting on Financial Statements of Employee Benefit Plans Subject to ERISA* (the proposed SAS).

Eide Bailly LLP operates in 13 states west of the Mississippi River and is the independent auditor for over 800 employee benefit plans (EBPs) for plan sponsors with small to middle-market businesses and not-for-profit organizations.

We support the Board's intent to improve the quality of EBP audits by strengthening the EBP auditor's report. We agree that the auditor reporting model for ERISA plan audits should be sufficient to produce a report that will clarify the audit procedures required and responsibilities of both auditors and plan management, thus addressing the requests from regulators and, perhaps alerting the unexperienced EBP auditor, and generally agree that certain proposed changes do improve the clarity of the report, particularly related to management and auditor responsibilities. We also believe that these new requirements will result in an increase in the amount of time, and thus cost, necessary to complete these engagements. Unfortunately, we also believe that there will continue to be a segment of practitioners that will not properly follow the proposed requirements, thus resulting in an unintended consequence of small-to-middle market plan sponsors engaging less qualified auditors, thus negating the objectives of the proposed standard. Accordingly, addressing the issue of the quality of work performed in EBP audits will not be solved alone by the adoption and implementation of the requirements as proposed.

Our key observations are included in this cover letter. Appendix I provides our specific comments on Issues 1-9 and content of the proposed SAS, as requested by the Board.

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## **Consideration of the Objectives of the Proposed Standard**

We are aware that the quality of many EBP audits has been found to be poor and the attempts to raise awareness, provide education, and improve the work product have fallen short for a large number of practitioners performing these engagements. We realize that more direct methods to impact quality need to be considered and proposing a standard specific to the performance of the audits of ERISA plans is a legitimate option. However, we are not convinced that the lack of quality in EBP audits is a function of the standards currently in place, rather a reflection of the failure to properly apply existing standards.

Accordingly, we are not convinced that simply modifying the auditor's report and adding specific compliance-type procedures will result in an improvement in auditor performance on these engagements. The fact of the matter is that auditors currently performing these engagements at an appropriate level of quality will continue to do so, and for the significant number of auditors that are not, their behavior will likely not be changed by the adoption of this proposed standard. In fact, a number of those auditors will continue to perform these engagements at an unacceptable level of quality and still issue a report consistent with that proposed by simply copying language from examples provided in third-party practice aids.

While there is merit in the proposed changes that address clarification of management's and the auditor's responsibilities, and clarification of the nature of a limited scope engagement, addressing auditor performance for these engagements will involve much more than a change in auditor reporting.

## **Risk Assessment Considerations**

Paragraph 15 of the proposed SAS begins with "Irrespective of the risks of material misstatement the auditor should perform substantive procedures for..." We are of the general opinion that auditor assessment of risks of material misstatement should always be a consideration in the planning and performance of an audit engagement, and that the variations in types and sizes of employee benefit plans, as well as the variation in plan provisions make it impossible to effectively and efficiently plan and perform an audit "irrespective of the risks of material misstatement".

A fundamental concept to the performance of any audit engagement is the auditor's assessment of risk and the related responses to those risks, thus we do not believe it is appropriate that the proposed standard include requirements absent a consideration of the risk of material misstatement. If such requirements are considered necessary by a regulator or others, perhaps an alternative type of engagement is more appropriate, rather than to include such requirements to the audit of the employee benefit plan financial statements.

## **Public Reporting by the Auditor**

Unique to large EBPs is the sharing of audited financial statements with the public on the EFAST2 Form 5500 reporting system. This site is open to the world, not just employers, participants and regulators. We do not believe it is the auditor's responsibility to provide information regarding a plan sponsor and/or plan trustees administration and oversight of an employee benefit plan. We do not necessarily disagree with requirements for an auditor to report findings to management and/or those charged with governance of a plan, or possibly to a regulator; however believe it is then those party's responsibility to provide necessary and appropriate information to other parties.

If you have questions about our comments, or wish to discuss the matters addressed in this comment letter, please contact Maria Christiaens at (406) 896-2438.

Sincerely,

*Eide Bailly LLP*

Eide Bailly LLP

## Appendix I – Comments on Issues 1-9 and Content of the Proposed SAS

### Issue 1 – Required Procedures When an ERISA-Permitted Audit Scope Limitation is Imposed

*Respondents are asked to provide their views on whether*

1. *the procedures and guidance will achieve the objectives of enhancing execution and consistency in these engagements and if not, why;*

**Response:** We believe that the procedures proposed in paragraphs 20—21 are consistent with our current practice. However, there could be clarification of paragraph 20(b) as to what a “qualified institution” would be and whether an all-encompassing “custodian” term can be used within the auditor report.

*and*

2. *any procedures that should be required are missing, and if so, describe them.*

**Response:** We believe it would be helpful to add discussion of the role of agents for the custodian in the Application Material.

### Issue 2—The Form and Content of the Auditor’s Report on ERISA Plan Financial Statements with the ERISA-permitted Audit Scope Limitation

*Respondents are asked to provide feedback on whether the form and content of the proposed auditor’s report, including the form and proposed content of the new form of opinion*

1. *provide improved transparency with respect to reporting on an audit of ERISA plan financial statements when an ERISA-permitted audit scope limitation exists, and if not, how could it be revised;*

**Response:** We agree that the proposed enhanced reporting does improve transparency of the roles in a limited scope audit.

2. *will improve the auditor’s understanding of his or her responsibilities in a limited scope audit resulting in potential improvements in audit quality, and if not, why;*

**Response:** We noted the proposed enhanced reporting was designed to give to the auditor credit for the work performed in a limited scope audit, specifically around the procedures related to investments. In the past, it was not always clear to the user what the auditor’s responsibilities were in a limited scope audit. With respect to potential improvements in audit quality, please see our comments above regarding the assumed linkage between auditor reporting and auditor performance. Accordingly, we believe the combination of more effective peer review and regulatory oversight will likely identify delinquent work more readily than the proposed changes in auditor reporting.

3. *better describe management’s responsibilities for the financial statements, and if not, why;*

**Response:** We agree the proposed new form of opinion better describes management’s responsibilities, especially surrounding investments.

4. *provide sufficient clarity to users with respect to the auditor’s responsibilities and matters reported, and if not, why.*

**Response:** As noted above, we generally agree that the proposed changes provide increased and sufficient clarity with respect to the auditor’s responsibility.

However, as we have also noted, we do not believe that the auditor’s report is the appropriate vehicle for the communication of findings with respect to outside parties. Rather, we believe it is more appropriate for the auditor to provide findings to management and/or those charged with governance, with communications to regulators and others to be provided by one of those two parties.

### **Issue 3—Modifications to the Opinion in the Independent Auditor’s Report**

*Respondents are asked for their views about the proposed interaction of AU-C section 705 and the proposed SAS when the ERISA-permitted audit scope limitation is imposed by management including*

1. *whether the guidance in paragraphs 31 and 34 of the proposed SAS (a) is clear with respect to the auditor’s responsibilities for addressing the circumstances described previously,*

*and*

*(b) achieves the objective of providing transparent reporting to the users, and if not, suggested revisions.*

**Response:** While we would prefer a less cumbersome approach than the development of a new AU-C section, we also do not have an alternate solution that achieves the same objectives without similar challenges.

2. *the form and content of the example reports (nos. 5–7) illustrating qualified and disclaimers of opinion regarding the application of the guidance in paragraphs 31 and 34.*

**Response:** We believe the form and content of the example reports adequately illustrate the proposed changes.

#### Issue 4—Required Emphasis-of-Matter Paragraphs

1. *Respondents are asked to consider whether the situations identified are appropriate for requiring the inclusion of emphasis-of-matters paragraphs in the auditor’s report.*

**Response:** We agree that the situations identified in Paragraph 116 of the proposed SAS are appropriate for inclusion of emphasis-of-matter paragraphs in the auditor report.

2. *Respondents are also asked to consider whether there are additional situations that should result in a required emphasis-of-matter paragraph.*

**Response:** We suggest that the termination of a Plan also be considered as a circumstance requiring inclusion of an emphasis-of-matter paragraph.

#### Issue 5—Reporting Internal Control Deficiencies

*Respondents are asked to provide feedback on whether*

1. *the current reporting of internal control deficiencies to those charged with governance is sufficient;*

**Response:** We do not have any specific comments related to the current reporting of internal control deficiencies or have items that we would specifically consider for change. The current standard applies to all audits and the changes that were made through the audit clarity standard enhanced this reporting sufficiently.

*and/or*

2. *there are other reporting considerations the ASB should evaluate.*

**Response:** We believe that the root cause of compliance findings are often reflective of related internal control deficiencies, for example, the lack of an appropriate or effective control environment. Accordingly if the ASB believes that there are compliance-type findings that are unrelated to the plan’s internal control environment, clarification and related guidance would be helpful to practitioners.

## Issue 6—Certain Requirements for Audits of ERISA Plan Financial Statements and Related Required Report on Specific Plan Provisions Relating to the Financial Statements

*Respondents are asked to provide feedback about the required procedures discussed in paragraphs 15–16, and the reporting of findings discussed in paragraphs 119–124 of the proposed SAS, including views regarding the following:*

1. *With respect to the required procedures in paragraphs 15–16*
  - a. *Will these requirements enhance the consistency and quality of the audit work performed relating to matters that could have a direct effect on the financial statements, including related disclosures, and if not, why?*
  - b. *Does the proposed SAS provide appropriate guidance on achieving these requirements, including*
    - i. *which provisions of the plan instrument should be tested; and*
    - ii. *to what extent testing should be performed?*
  - c. *What procedures related to other plan provisions or specific areas of the financial statements should be included in the required testing to enhance the usefulness of the proposed reporting of the findings?*

**Response:** As the requirements in these paragraphs are to be performed “irrespective of the risks of material misstatement”, they certainly should be expected to result in consistency of audit work performed. However, as we have stated elsewhere in this response, we are skeptical that such an approach will result in a corresponding increase in the quality of audit work performed.

With respect to whether the proposed SAS provides appropriate guidance on achieving these requirements, we are concerned that the “irrespective of risks of material misstatement” approach does not appropriately consider the existence of variations in types and nature of plans, variation in plan provisions, and other factors.

We do not believe there are other plan provisions of specific areas of the financial statements that should be included as required testing.

2. *With respect to reporting on the findings resulting from performing procedures related to the areas in paragraphs 119–124, whether there are opportunities to enhance the proposed requirements and guidance including whether:*
  - a. *Including the list of individual areas tested is appropriate and if so whether there are other items that should also be included (if not, why not).*

**Response:** As we have stated, we do not generally support the inclusion of findings by the auditor as a part of the auditor’s report. However, should such a requirement be included in a final SAS, we agree that including the list of individual areas tested is appropriate

Overall, if auditors are required to include in testing all of the items that are noted in the paragraphs referenced above, without any regard to materiality and/or risk, this will result in an increase in the amount of time necessary to complete these audits.

- b. *The requirement to exclude findings that are “clearly inconsequential” is appropriate, and if so is there guidance the ASB can consider to drive consistency in application in practice?*

**Response:** Yes, the requirement to exclude “clearly inconsequential” is appropriate. However, in practice this will be very difficult to apply consistently, especially if as noted in paragraph A136, the auditor and client may reach an agreement in advance on the nature of findings that would be considered clearly inconsequential.

Given that a conclusion as to nature of finding being “clearly inconsequential” involves auditor judgment, we believe it will be difficult for ASB to provide specific guidance. We believe the best opportunity for the Board to provide guidance may be to provide examples of the type of finding that would reasonably be considered to be “clearly inconsequential” and include those in the Application Material and/or subsequent supplementary guidance materials.

- c. *The findings should also include any matters identified by management or the plan administrator? [Note: As currently drafted, the proposed SAS requires the auditor to include findings that were noted as part of the auditor’s work performed in relation to paragraphs 15–16.]*

**Response:** No – matters identified by management or the plan administrator should not be included, as we do not believe it should be the auditor’s responsibility to communicate information on the behalf of management.

- d. *The reporting illustrations included in the Exhibits to the proposed SAS specific to reporting the findings are clear and result in sufficient information to the user of the report?*

**Response:** Yes, we believe the reporting illustrations are clear.

- e. *There may be unintended consequences from including the findings in the auditor’s report, and if so, what those unintended consequences may be and how might they be mitigated?*

**Response:** As noted in our introductory comments, we believe there is a potential unintended consequence related to the appropriate application of the proposed additional requirements by some auditors resulting in an increase in fees charged, which then could result in plan trustees hiring auditors that are not appropriately applying the proposed requirements, thus the intended result of an overall increase in quality will not be achieved.

- f. *there are alternatives to reporting the findings in the auditor’s report that would achieve the objectives related to enhancing audit quality?*

**Response:** We believe that consideration should be given to only reporting repeat findings which the plan sponsor hasn’t addressed, and/or the reporting of findings in a separate report, which would be filed at some time after completion of the audit and require the inclusion of management’s responses and corrective actions.

3. *Whether the required additional procedures and reporting of findings will result in additional costs, and if so, views as to the extent of those costs and whether they outweigh the potential benefits of enhanced audit quality?*

**Response:** We believe that the proposed requirements will result in additional costs, considering the proposed requirement that procedures be performed irrespective of risks of material misstatement, and for the reasons that have included in our response, that it is questionable whether the benefits of this approach will exceed those costs.

## Issue 7—Required Procedures Relating to the Form 5500

1. *Respondents are asked for their views about whether the proposed procedures in paragraphs 36– 48 of the proposed SAS would achieve the objective of increased consistency with respect to identifying information in the Form 5500 that may be relevant to the audit of ERISA plan financial statements, and if not, why?*

**Response:** We noted the proposed procedures mirror those found in AU-C Section 720, paragraphs .06 through .18. We find the comments in the application and other explanatory material paragraphs A6 through A76 are tailored in a helpful manner for the Form 5500.

This area is extremely important going forward as the DOL has announced its intent to make sweeping changes to the Form 5500, after which the requirements of the proposed SAS would require even more significantly detailed reporting for the auditor to consider, adding even more time and cost to these engagements.

## Issue 8—Proposed New Reporting Standard and Amendments to Other AU-C Sections

*Respondents are asked whether*

1. *the proposed approach of creating a new reporting model for reporting on ERISA plan audits (AU-C section 703) will better describe management’s and the auditor’s responsibilities in these engagements;*

**Response:** We believe that the proposed model does appropriately and more clearly describe management’s and the auditor’s responsibilities in these engagements.

2. *the proposed amendments to the other AU-C sections are appropriate;*

**Response:** The proposed amendments to other AU-C sections appeared to be appropriate.

*and*

3. *whether there are other sections of AICPA Professional Standards that might need to reflect the provisions of this proposed SAS.*

**Response:** We did not identify any other sections of AICPA Professional Standards that will require changes related to the provisions of the proposed SAS.

## Issue 9—Proposed Effective Date

1. *Respondents are asked whether the proposed effective date provides sufficient time for preparers, auditors, and others to adopt the new standard and related conforming amendments.*

**Response:** We believe that the proposed effective date does not provide sufficient time for auditors and others to adopt the proposed SAS and related conforming amendments. We believe it will take a considerable amount of time for service providers such as PPC and CCH to prepare the necessary materials and guidance for auditor application of the requirements in the proposed SAS. Additionally, we believe the timing should be coordinated with the potential Form 5500 modernization changes.